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PAUL W. COBB, JR.

June 11, 1997

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*Federal Communications Commission  
Office of Secretary*

**VIA MESSENGER**

**DOCKET FILE COPY ORIGINAL**

William F. Caton  
Acting Secretary  
Federal Communications Commission  
1919 M Street, N.W., Room 222  
Washington, D.C. 20554

Re: In the Matter of Access Charge Reform, CC Docket No. 96-262/Price Cap Performance  
Review for Local Exchange Carriers, CC Docket No. 94-1

Dear Mr. Caton:

Enclosed please find five copies of three documents that MCI Telecommunications Corporation cited in its Opposition to the Joint Petition for a Partial Stay that was filed on Monday, June 9 in the above-captioned matter. Please add these documents to our submission. We are providing copies of the documents to the Commission to facilitate its consideration of our filing.

Thank you for your assistance. Please call me if you have any questions. My telephone number is 202/637-6399.

Sincerely,

*Paul W. Cobb, Jr.*  
Paul W. Cobb, Jr.

Enclosures:

1. The Yankee Group, "The Unbearable Lightness of Local Competition," 14 *Consumer Communications* 2 (1997) (cited on p. 28 of MCI's June 9, 1997 Opposition to the Joint Petition for a Partial Stay).
2. Affidavit of Kenneth C. Baseman and Frederick R. Warren-Boulton on Behalf of MCI Telecommunications Corp. (Exhibit A to the June 10, 1997 Comments of MCI Telecommunications Corp. in CC Docket No. 97-137) (cited on p. 28 of MCI's June 9, 1997 Opposition to the Joint Petition for a Partial Stay).
3. Comments of MCI Telecommunications Corp. in CC Docket No. 97-121 (May 1, 1997) (cited on p. 29 of MCI's June 9, 1997 Opposition to the Joint Petition for a Partial Stay).

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# The Unbearable Lightness of Local Competition

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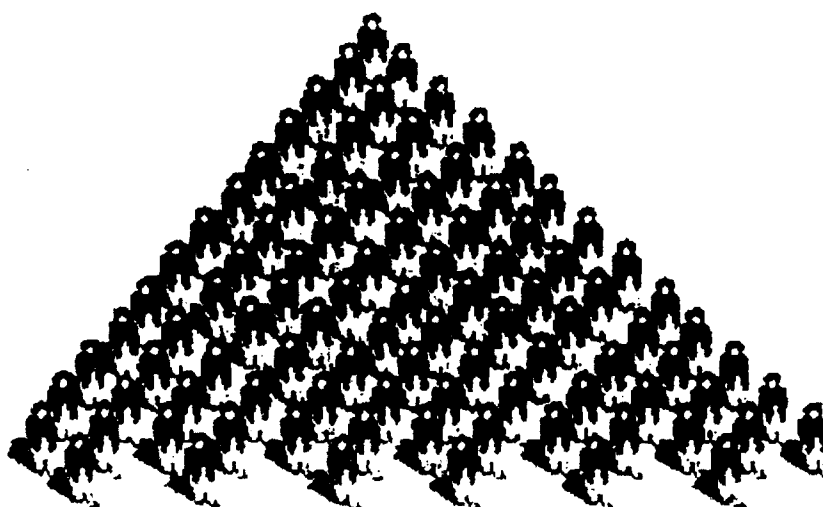
## Executive Summary

Recently, many parties with a vested interest in the outcome of the RBOCs' 271 filings for in-region long-distance authority have expressed skepticism as to the effectiveness of the Telecommunications Act of 1996 in introducing true competition to the local market. The RBOCs' entry into in-region long distance hinges on the interpretation of the language in the Act that calls for the existence of a facilities-based carrier, the completion of the 14-point checklist, and consideration of the "public good." While the RBOCs are close to meeting the 14 points on the checklist, there is actually very little competition in the local residential market (see Exhibit ES-1). To many competitive local exchange carriers (CLECs), Total Service Resale (TSR) is not as attractive as a local entry strategy, and many issues surrounding interconnection and Unbundled Network Elements (UNEs) remain unresolved. What, then, can we expect in the months to come in the local market?

### Exhibit ES-1

#### Estimated Number of Consumer Households with Competitive Local Service

Source: the Yankee Group, 1997



LECs  
97 Million

CLECs  
0.5 Million

## Is There Competition in the Local Telecommunications Market?

The overwhelming majority of consumers in the United States still have no choice when it comes to picking a local phone company. The passage of the Telecommunications Act gave many hope that robust competition would quickly develop in the local telephone markets. Over a year has passed and local phone competition is scarce, especially in the residential market. In the local business markets, there are a myriad of CLECs providing services in major, and even secondary urban markets, but they account for only approximately \$1.9 billion in revenues, as compared to \$94 billion in revenue for the incumbent local exchange carriers (ILECs). The Yankee Group recently conducted a survey of telephone service providers either serving or intending to serve local telephone markets in the United States. The results of this survey indicate that there is proportionately very little local competition outside of urban areas, and the use of TSR as an entry strategy for the local markets is being pursued somewhat begrudgingly by CLECs.

The mechanisms for introducing ubiquitous local competition in the near term, namely TSR and UNEs, have been fraught with difficulties ranging from acrimonious interconnection negotiations to public displays of frustration over RBOC provisioning capabilities. While local competition develops with the speed of shifting tectonic plates, the RBOCs are anxiously anticipating long-distance authority. Already two filings have been submitted to the Federal Communications Commission (FCC), and many more are expected to follow.

### 271 Filings: Are the Impediments to Competition Removed from the Local Market?

The RBOCs' authority to offer long distance in-region does not explicitly hinge on the existence of a certain level of local competition. Rather, to gain long-distance authority an RBOC must prove that sufficient safeguards are in place that will ensure competition can exist. In short, RBOCs must show the existence of a facilities-based provider, offer service to residential and business customers, pass the 14-point checklist, and prove that their filing will serve "the public good." Based on the Yankee Group's interpretation of the Act, we believe that conditions exist in several states that meet at least the minimum requirements of the existence of facilities-based competition. Several of the RBOCs are close to compliance with the 14 points on the competitive checklist. **The FCC and the public utilities commission (PUC) must determine whether the impediments to competition have been sufficiently eliminated to the degree that the public interest would be best served by the RBOCs' immediate entry into in-region long distance.**

In reviewing the RBOCs' 271 filings, the regulators must balance the potential consumer benefits that would come as a result of the RBOCs' entry into long distance with the need for establishing adequate assurances against anti-competitive behavior on the part of the RBOCs in the local market. It does not appear that in any state today there are sufficient competitors outside of urban areas with enough market power to discipline an RBOC that was acting monopolistically. Yankee Group research shows that this lack of ubiquitous competition is caused both by the RBOCs and the difficulties in establishing adequate operational support system (OSS) interfaces, as well as by the lack of interest on the part of many CLECs in serving the mass residential market via TSR.

## **The Local Market: Finding Competition Depends on Where You're Looking**

In market-based terms, local competition will exist when a significant percentage of customers and resellers have a choice of local carriers. The question of whether or not there is competition in the local market today depends largely on how widely the market is defined. If one were to ask a Telecommunications manager at a Wall Street brokerage firm whether he had a choice of local telecommunications provider, the answer would be yes. If you asked a stock broker who lived in Hartford, Connecticut, if she had been offered a choice of local phone company, she might say yes, but if you asked consumers in the United States the same question, the overwhelming majority would most likely say no.

Local telephone competition cannot be described in terms of existing or not, but rather in terms of degree of competition and the potential for competition. There is some competition in high density, urban, business, and local markets. If it were possible to restrict the RBOCs to offering long-distance only in those areas and to those market segments where competition existed, a case could be made for their release (e.g., NYNEX could be allowed to offer long distance to business customers in Manhattan, but not residential customers in Westchester County, NY). Procedures in place today, however, are designed to grant the RBOCs long-distance authority for markets throughout a state. Today, if RBOCs were allowed into the long-distance market statewide, they would be competing for a customer's combined local and long-distance traffic in areas where there is no local competition—and that is clearly not in the public interest.

## **The RBOCs and Control Over the Local Market**

**If the RBOCs were granted authority to offer ubiquitous long-distance service in their regions today, the long-distance revenue streams of many major interexchange carriers (IXCs) would be decimated.** Previous examples of local companies offering long distance in-region without corollary local competition, such as in SNET and GTE territories, have shown that the long-distance companies will lose significant market share (as much as 25-30%) relatively quickly.

We already know that the large IXCs will lose some long-distance market share when the RBOCs enter the market. The Act is framed in such a way that the IXCs should be able to capture a portion of the local market in recompense. The difficulty in this arrangement is that local markets are far more complex, difficult to serve, and isolated. The CLECs, especially the major IXCs, are having a difficult time with interconnection, OSS Interoperability, collocation, and resale arrangements, and are currently not in a position to be able to take substantial quantities of local market share from the RBOCs. The RBOCs, on the other hand, having seen the success of companies such as SNET, GTE, Frontier, and others in gaining long-distance market share relatively quickly, are in a position to substantially impact the long-distance market upon their entry.

## **Liberating the Local Markets**

The local markets will be liberated as soon as the RBOCs are structurally prevented from displaying hegemony over the CLECs. As with most legislation, the Telecommunications Act of 1996 included a series of compromises, designed to help

foster competition without unduly helping or burdening any party. As it pertains to local competition, the Act is designed to create an environment where local competition can flourish. Recognizing that the RBOCs hold substantial market power, the 14-point checklist is not a definition of what local competition is, but rather a list of checks against potential market abuses by a dominant provider.

The liberalization of the local market, as laid out in the Telecommunications Act of 1996, is a complex endeavor. The local markets that regulators are trying to liberalize contain the remnants of a subsidy system that reflects the biases of a monopolistic, regulated market. When AT&T severed itself from the Bell System, it took with it the high growth, high margin, plum parts of the business—long distance and equipment manufacturing in particular. It left its Bell progeny with the dirty business of providing phone service to the masses, rate disparity between business and residential services, and an access rate structure that compensated it for its burdens.

The Bell System is over 100 years old, and should not be expected to turn itself into a nimble competitive supplier overnight. The liberalization of local markets will take time. And due to the complexities inherent in the local markets, it may take much longer than it did in long distance.

The implementation of equal access for long distance provides a good example of the difficulty in changing from a monopoly to a competitive market. In December 1984, 3.1% of the access lines in the United States had equal access, meaning that a customer could choose from several long-distance carriers without having to dial additional digits to reach a competitive network—three years later, 75.9 % of access lines had equal access. While this is a significant improvement, it demonstrates how difficult and time consuming it is to adapt a monopoly network to a competitive environment.

After three years, only three-fourths of consumers had a true choice in deciding on a long-distance provider, and equal access was a simple endeavor compared to the changes to the network that are necessary to open local markets. Additionally, the LECs had a financial incentive to implement long-distance equal access—every time a customer changed long-distance carriers, the local company received a switching fee. The opening of the local market holds no such direct incentive, rather only a promise of future long-distance revenues.

The task at hand today for regulators is not necessarily to prove that there is unabated local competition—as there is not. The question for the FCC is, are there sufficient restraints on the RBOCs to allow them entry into long distance? Have the barriers to competition been removed? Eventually, the FCC would like to see the restraints on the RBOCs administered by their competitors, not by regulators. This is why regulators have structured the long-distance entry criteria to include the existence of a facilities-based competitor, and equal access to all components of the local infrastructure.

The primary example of facilities-based carriers will be the non-IXC CLECs serving the business markets in major metropolitan areas. The non-IXC CLECs have had the easiest time signing interconnection agreements, and provide the best examples of true competition in their markets.

### **Coverage Criteria: Open One Market and Get the Whole State?**

The Yankee Group estimates that in the residential market, once the RBOCs are

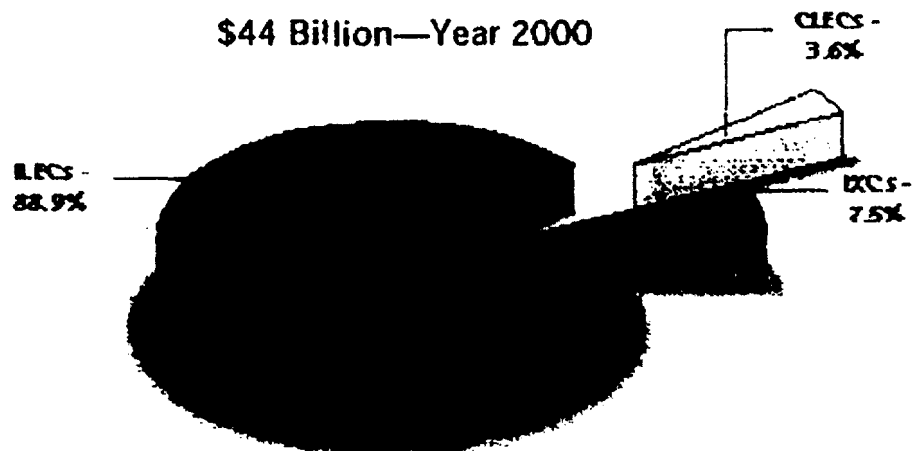
allowed to enter in-region long distance, their market share will reach up to 20% of the access lines within two years of entry. Local market share swings will be significant in some areas, and not in others. In the aggregate, market share swings will not be as dramatic in the local market. Exhibit 1 shows the estimated market share of CLECs and IXCs in the year 2000 for the combined business and residential markets. It is important to point out that the CLECs and IXCs will be selective in terms of their market entry, meaning their market share gain in particular segments will be much higher than the aggregated market share shown.

One of the fundamental difficulties in assessing when the RBOCs should be allowed into long-distance stems from the inherent differences between the local and long-distance markets. Entering the long-distance market, an RBOC can take full advantage of what competition has wrought—a healthy wholesale market for long distance. The RBOC can choose the most favorable rates, terms, and conditions from several competing facilities-based carriers. And when an RBOC is ready to enter long distance, essentially it can flip a switch and begin offering the service to an entire state the next minute. Most RBOCs have already entered into wholesale agreements with facilities-based long-distance carriers to provide underlying long-distance capability once the authority is granted.

The addition of RBOCs will make the long-distance market more competitive. The RBOCs have tremendous brand awareness, local presence, rock bottom wholesale long-distance rates, and healthy advertising budgets. In any given state, the RBOCs' brand will be powerful enough to drive instant acquisition throughout the state.

The path to becoming a long-distance reseller is well charted. Non-RBOC LECs such as GTE, Consolidated Communications, Citizens Telecommunications, and others have shown that there is a strong proclivity for extending local phone service to include long distance. These companies have been able to garner substantial market share in long

**Exhibit 1**  
**Business and Residential Local Exchange Market**  
*Source: the Yankee Group, 1997*



*Note: CLEC revenues exclude MFS and MCI metro; revenues for dial tone only, EULC, taxes, and tolls are not included.*

distance in a short period of time.

In contrast, the local market must be entered into in increments, market by market. RBOCs and regulators will be able to identify at numerous cities and metropolitan service areas (MSAs) that have a rich diversity of competitive providers. However, in no state is there a facilities-based provider, other than the incumbent, that can serve the entire state. Thus, we are left with the quandary: Should an RBOC be able to offer long distance in a whole state, if it can prove competition only in a few MSAs?

The solution, according to the Act, is to require TSR as a means for a competitor to enter the entire state with a local service offering. Unfortunately for the long-distance companies, the liberalization of the local markets allowed them access to a market that they were not initially interested in. The prospect of reselling voice traffic (a mature market) to residential consumers (who are used to flat rate pricing and unlimited local use) over another company's network, at rates that do not allow for good profit margin, would almost be comical if it were not absolutely necessary in order to protect the core long-distance market. Our research shows a definite ambivalence to serving the local residential market via TSR by any entity save the IXC's, and their collective interest stems from self preservation.

In the case of resale, the potential local competitor has only one choice for its underlying wholesale capability—the local exchange carrier (LEC). In a truly competitive and open market, a potential entrant would have the option of at least one other alternative to the LEC. The competitor using TSR ends up, in effect, acting as a sales agent for the RBOC network.

## **The Trouble with TSR**

TSR should be thought of as a means to get to a competitive local market, but does not allow for true and open competition. This will develop only when customers and resellers have a choice of facilities-based local carriers. Without the presence of a facilities-based alternative, the ILEC possesses too much market power, and is an impediment to competition.

TSR is an appropriate bridge to competition, but cannot facilitate true competition because it does not give the competitors a means to differentiate their services on anything but price. Because the incumbent possesses the entire "product," and is offering it to all potential competitors, customers cannot receive anything different beyond what the ILEC has already offered. For this reason, the IXC's entering the local markets will use resale as a temporary vehicle to obtain customers. As quickly as is feasible, they will take advantage of Unbundled Local Elements.

All of the IXC's that we interviewed for this White Paper indicated that their economic justification for serving any market hinged on favorable UNE's terms. Purchasing UNE's, particularly the local loop portion, will allow the IXC's to differentiate the services they provide to the end user, as well as control substantial portions of their cost (most importantly, access). Because UNE's will be used in many situations where the IXC as a CLEC has deployed a local switch, many of the first residential customers to be serviced by the IXC's in this manner will be those in proximity to the businesses they serve.

The RBOCs have argued that UNEs is unfair and not in the spirit of the Act because it doesn't present an incentive to competitors that are building their own networks. The Yankee Group has found that many potential competitors find suitable justification to install their own switches simply to control their own destiny and avoid reliance on the RBOCs. For most potential competitors, UNEs is a means to get to the most coveted portion of the network, the local loop.

The RBOCs argued that the UNE provisions of the FCC's ruling on interconnection forced them to sell services at or below cost, which represented confiscation of property, and therefore was unconstitutional. For this reason, many of the provisions of the FCC interconnection order were stayed. Competitors continued on, despite the stay, to develop interconnection agreements without the benefit of standardized pricing.

### **Market-Based Definition of Competition**

While the regulators have the difficult task of assessing the wisdom of allowing RBOCs into long distance, the Yankee Group has the luxury of assessing local competition from a market-based perspective, as well as a regulatory and legal viewpoint.

The RBOCs are in control of the local infrastructure. The 14-point checklist, and the interconnection arrangements that the RBOCs have entered, describe the methods that the competitors will use to rent portions of this infrastructure, but it remains the property of the RBOCs and under their control. This points to a critical component of true competition that is lacking in most residential markets. The competitors cannot substantially control their supplier's costs, and they have no alternative that would allow them to inflict market discipline.

OSSs are critical to local competition. These are the systems through which competitors preorder service, provision, conduct maintenance, handle customer problems, get billing information, and manage customer information. Much of the delay in the roll out of local service via TSR is due to the problems competitors are having with RBOCs' OSSs. The OSSs in place today were designed for a single user. The RBOCs' systems were not meant to accommodate multiple users, and this is causing problems.

The bare minimum for competition in the local markets includes OSS interoperability so that the incumbents systems and any potential competitors are at parity. This means that benchmarks should be established and reported to ensure that customers of the incumbent RBOC are not given preferential treatment. The quality of local service depends on the quality of these interfaces. If the interfaces are insufficient, the business support processes of the competitive LEC will suffer, and delays will result.

Not one company that we spoke to had a favorable impression of the OSS capabilities of the RBOCs. The IXC's, in particular, have been very vocal as to the level of OSS interoperability they expect and are currently receiving. The CLECs indicated as well that they had experienced difficulty, but the nature of their interconnection with the RBOCs was such that they were not as reliant on these systems.

Processing provisioning orders in bulk is somewhat of a "chicken-and-egg" situation for the RBOCs and IXC's. The IXC's cannot prove that the RBOCs' OSSs are unacceptable unless they can push the limits by attempting to process a large number of orders, but they cannot get a large number of customer orders until the systems are in place to process them. Thus, we have the "war of words" between the concerned parties, while



in the background the RBOCs struggle to de-antiquate their system and the IXC's to build their own local OSS's to prepare for the big push into the residential markets.

### Different Criteria for Business versus Residential

The long-distance and local phone companies are anxious to take advantage of the unactualized preference of both businesses and residential consumers to deal with a single service provider. As Exhibit 2 demonstrates, competition in the different markets will proceed with varying speeds, with the large business markets seeing the most growth in competition.

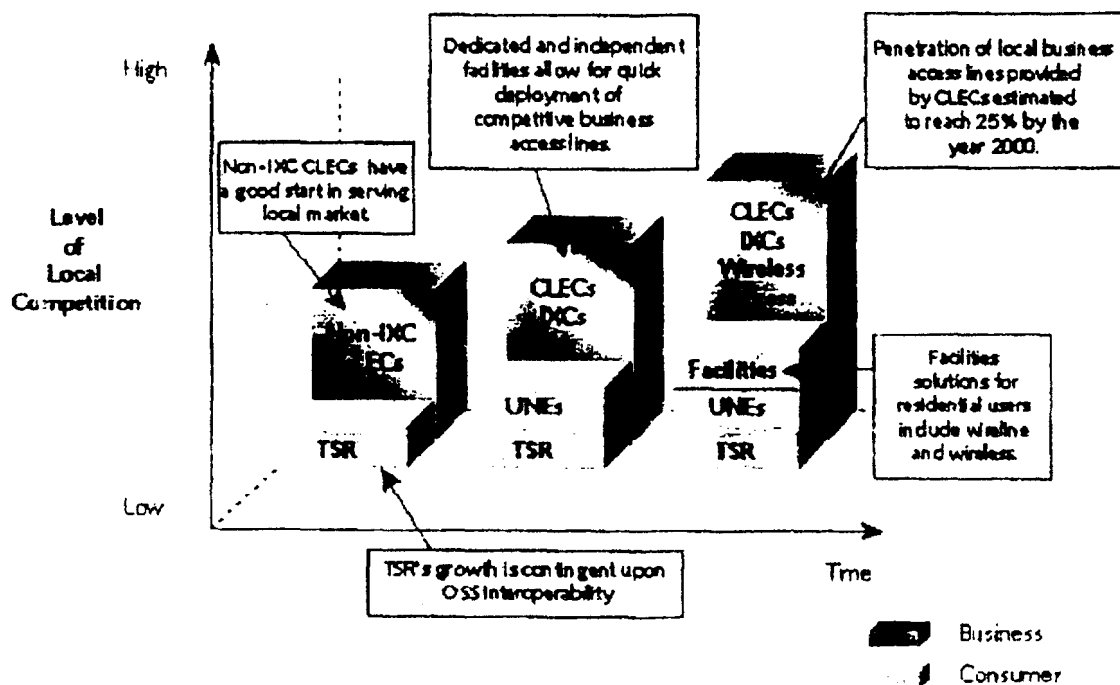
To residential consumers, the expectation for local competition is that it will bring simplicity and lower prices. Simplicity will come from dealing with one company for both local and long-distance service. The Yankee Group's Technologically Advanced Family (TAF) Survey indicates that 67.4% of households would be interested in dealing with a single provider of telecommunications services.

There has also been a good deal of expectation that residential rates for local phone service will decline with the advent of competition. Consumers may be somewhat disappointed in the actual level of price decreases that will initially occur in the local market. Local rates are not likely to drop precipitously because:

- The RBOCs have no incentive to drop rates as long as they are compelled to resell their services at a percentage off of retail.
- The RBOCs claim that, in many cases, residential retail rates are already below cost.

### Exhibit 2 Business and Residential Competition

Source: the Yankee Group, 1997



- The discount rates that have been established for resale do not allow for significant price decreases. The margins on local service will be quite small. The IXC's were requesting resale rates in the 40 to 50% range. Resale rates of 17 to 25 % do not allow for much discounting.
- The RBOCs are losing portions of their revenue stream as a result of recent access reform, making them less likely to lower rates in non-access areas.

Residential consumers have not stood up and demanded facilities-based competition. The potential benefits of competition—better customer service, more choice, and lower rates—are not absolutely tied to facilities. However, for a company to enter the local market, it must be attractive from an economic standpoint. In the long run, for large companies, TSR is less attractive economically than UNEs or facilities-based competition.

It is not surprising then to see the long-distance companies enter the local residential consumer markets with some trepidation. AT&T's and MCI's limited market entry demonstrate the unattractiveness of TSR—especially when the poor economics are combined with unsettled OSS issues. The IXC's will enter the local market in a broad way when the OSS issues are resolved, and their own local systems are in place.

## Who Will Serve the Residential Markets and How?

Competition in the residential local markets will be driven by two primary forces. First, the IXC's and resellers will enter the local markets in order to protect their core markets. Secondly, facilities-based competition in the local residential market will emerge as CLECs that build networks primarily to serve business customers look for methods to further utilize their investments. Facilities-based residential competition will occur first in the high density urban areas where residential customers can be reached by CLEC networks.

This pattern of market penetration will be similar to the evolution of the long-distance market. Competitors in long distance began by building portions of their own networks, and leasing the rest in order to service business customers. This led to increased investment in networks. At the point that the networks were near completion, companies emphasized increasing minutes on the networks by adding residential customers.

## IXCs: Defense and Access Avoidance

Wide scale competition for the local residential market by IXC's is contingent upon improving the OSS interfaces with the RBOCs, and developing attractive rates for UNEs. The companies we interviewed indicated that TSR is only a short-term strategy, and economically, UNEs is the method they will use to reach the suburbs. LCI, MCI, Sprint, and AT&T all indicated that their current level of involvement in the residential markets could be characterized as limited. The key to their long-term economic viability lies in the rates for the unbundled local loop and other network elements, and the avoidance of access charges for long distance. The economic model that is driving the IXC's is tied intrinsically to access cost avoidance, as well as long-distance market protection.

## **Non-IXC CLECs**

Most CLECs interviewed for this White Paper are not interested in serving residential customers directly. In general, CLECs will provide service to residential customers where they are legally compelled to do so, or via wholesale arrangements. For example, WorldCom, formerly MFS, sells capacity to RCN, which in turn serves the residential market. WorldCom provides the network, and RCN maintains the retail relationship with the customer. This type of arrangement will be the most typical method for CLECs serving residential customers. Some of the CLECs anticipate over time, if they have excess network capacity, that they will service some residential customers directly, primarily in large residential buildings. In any case, unless regulation requires otherwise, the CLECs primary motivation is to serve all of their customers, whether business or residential, with as little interface with the LECs as possible.

## **Shared Tenant Services Providers**

The most apparent example of competitive provision of residential local services today is the burgeoning STS market. Shared Tenant Services (STS) providers are companies that provide telephone, cable, Internet, and other services to large complexes of residential customers. Examples of STS providers include GE Capital Rescom, Optel, RCN, and MTS. These companies have evolved from providing private branch exchange (PBX) solutions for telephony to the point where many of them today are purchasing their own local switches.

These service providers do not have any interest in offering service via TSR. Instead, they want to capture customer revenues by leveraging their relationships with building owners. In many cases, the STS providers and building owners have developed rather strong business relations that may make it difficult for entrenched local or long-distance carriers to recapture these customers' communications purchase decisions.

The Yankee Group believes that STS providers are strong niche player competing for loyalty in a market segment that totals approximately 16 million households. However, the total number of apartment dwelling consumers that are currently served by someone other than their incumbent LEC is less than 300,000. Furthermore, due to capital requirements and continued technological obstacles, we believe that STS providers will capture no more than 700,000 million subscribers by the year 2000. While not ubiquitous by any means, competition in the STS market is as close to real facilities-based residential competition as you can get in the United States today.

## **Cable Companies**

Cable companies, once thought to be the most logical first competitors to the RBOCs in the local markets, have backed off their initial grandiose plans for telephone competition. Today, there are only a handful (less than 10,000) of customers receiving local phone service from their cable company. Although not as widespread as initially anticipated, eventually there will be more competition in the form of hybrid fiber/coax (HFC) networks delivering cable and telephony over the same plant.

Cox Cable Communications, Jones Intercable, Continental Cablevision (now part of U S WEST Media Group), and Time Warner are the best examples of cable MSOs with

plans to offer a substantial portion of their cable subscribers' local telephony service. However, their frustration in dealing with the RBOCs is apparent as companies such as Time Warner have put all telephony initiatives on hold until greater clarity surrounding the Telecommunications Act is provided. In fact, this frustration provides further validation for cables' overall plan to offer telephony over their own facilities with as little reliance on the LEC infrastructure as possible.

### **And Finally, A Word on Access Reform**

One of the major hurdles to many CLECs' business plans was removed, at least partially, with the FCC's announcement of the structure of access reform. Almost as important as the specific details in the decision is the fact that one was reached, and the conditions were articulated. This will allow IXCs and other CLECs to understand their costs going forward as they pertain to access. Without this understanding, the CLECs could not completely know the economic viability of their local entry strategies.

The access reform decision was clear in that it avoided associating access charges with UNEs. This is a clear indication that the FCC's intention is to promote local competition through UNEs and facilities. The announcement of the access structure was a major step in clearing the path for more robust local competition, and in the months to come we can expect to see increased activity on the part of the CLECs. The local markets are now much closer to being shaped by market forces, and less on regulation.

---

## Further Reading

"Local Number Portability: You Can Take It With You." *Yankee Watch Consumer Communications*, Vol. 14, No. 1, January 1997.

"Local Competition: One Step Closer," *Yankeevision Consumer Communications*, Vol. 13., No. 16, August 1996.

"The Telecommunications Act of 1996: A Legalized Free For All," *Yankeevision Consumer Communications*, Vol. 13, No. 3, February 1996.

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**JUN 11 1997**

**Federal Communications Commission  
Office of Secretary**

**BEFORE THE  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554**

In the Matter of	)	
	)	
Application of SBC Communications,	)	
Inc. Pursuant to Section 271 of the	)	
Telecommunications Act of 1996 to	)	CC Docket No. 97-121
Provide In-Region, InterLATA	)	
Services in Oklahoma	)	

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May 1, 1997.

### **EXECUTIVE SUMMARY**

MCI Telecommunications Corporation (“MCI”) opposes the application of SBC Communications, Inc., and its subsidiaries Southwestern Bell Telephone Company and Southwestern Bell Long Distance (collectively “SWBT”) to provide originating interLATA services in Oklahoma pursuant to section 271 of the Communications Act, as amended by the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (“1996 Act” or “Act”). SWBT’s application should be denied because it has not met the statutory requirements for providing in-region long-distance service: SWBT has not entered into an approved agreement with a competitor providing predominantly facilities-based service to residential and business customers that fully implements each of the items on the competitive checklist; SWBT has not met the separate affiliate requirements of section 272 of the Act; and SWBT’s entry into the long-distance market in Oklahoma would be contrary to the public interest.

1. SWBT has not entered into an approved agreement with a competitor providing predominantly facilities-based service to residential and business customers that “fully implemented” each of the items on the competitive checklist, as section 271 expressly requires. SWBT nevertheless argues that its entry into the long-distance market is required because it has “offered” or “made available” the items on the competitive checklist in an agreement with Brooks Fiber Communications and in a Statement of Generally Available Terms and Conditions (“SGAT”). *See, e.g.,* Brief in Support of Application by SBC Communications Inc., et al., for

Provision of In-Region, InterLATA Services In Oklahoma (filed April 11, 1997) ("SWBT Br."), at 12-17. This is a transparent attempt to avoid the explicit requirements of the Act.

"Track A" of section 271 (§ 271(c)(1)(A)) requires a Bell Operating Company ("BOC") to show more than that it has entered into a contract reciting the competitive checklist. The BOC must demonstrate actual competition through working interconnection agreements that "fully implement[]" all of the checklist items. §§ 271(d)(3)(A), 271(c)(1)(A). SWBT must therefore establish, among other things, that services have been provided in a timely and nondiscriminatory manner, in volumes adequate to satisfy the commercial needs of customers, and of a quality equal to that which SWBT provides itself.

SWBT does not even claim to be commercially providing, let alone fully implementing, all 14 checklist requirements. Indeed, SWBT's filing is little more than a list of *promises* to provide checklist items sometime in the future, using systems and methods not yet developed. For example, SWBT promises to provide state-of-the-art operations support systems ("OSS"), SWBT Br. 24-28, but at this time its OSS is largely untested and has not been commercially used by competitors. As a result, the Commission can only speculate whether competing providers can order service and unbundled elements on a reliable, nondiscriminatory basis. Similarly, there is not a shred of evidence that SWBT has even begun to implement -- let alone fully implemented -- numerous checklist requirements such as access to unbundled switching, Advanced Intelligent Network databases, or combinations of unbundled elements. There is no evidence of technical specifications, tests, trials, or commercial use of these complex systems.

SWBT's application is also premature because cost-based prices have not been established for network elements as required by the Act. Indeed, SWBT has reserved its right to challenge the basic notion of determining costs in Oklahoma using "TELRIC" methodology -- and has already challenged in federal court in Texas the legality of basing rates on TELRIC -- leaving uncertainty not only as to the level of final prices, but also as to whether TELRIC methodology will ultimately be used to establish prices. In the meantime, the interim rates established in Oklahoma are far higher than forward-looking cost-based rates required for compliance with the Act, and higher even than the interim proxy rates established by the Commission.

Unable to satisfy Track A, SWBT falls back on Track B (§ 271(c)(1)(B)). But SWBT cannot comply with the Act by relying on what is essentially a tariff. Track B allows for compliance via an SGAT only in the exceptional circumstance where competing providers refuse to request access at all. But as SWBT admits, several agreements with competing providers had already been *approved* by the OCC before January 11, 1997 (*i.e.*, three months prior to SWBT's application, the relevant date under Track B). SWBT Br. 4-5 & nn.3-4. Thus, compliance by means of an SGAT is not available to SWBT as a matter of law.<sup>1</sup>

2. SWBT has failed to demonstrate that it will comply with the separation and nondiscrimination requirements of section 272. Instead of providing information explaining how

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<sup>1</sup> Track B is also available if the state commission issues a finding that competing providers refused to negotiate in good faith, or failed to comply with the implementation schedule in the applicable interconnection agreement. There has been no such finding -- and no such allegation by SWBT -- in Oklahoma.

it will comply, it merely repeats the language of the statute and the Commission's implementing regulations. These boilerplate statements are insufficient to demonstrate compliance with section 272.

3. SWBT's application is also premature because its local bottleneck is firmly in place. Congress understood that it is not in the public interest for a BOC to enter the in-region long-distance market until there is effective local competition. Operations of a few new entrants who serve only a handful of customers in two Oklahoma cities do not impose any effective marketplace constraint on SWBT's exercise of its continuing monopoly power. Moreover, the lack of any serious competitive presence permits SWBT to continue to charge long-distance providers access charges that are many multiples of SWBT's cost. These inflated access charges fund what amounts to a war chest -- derived from its bottleneck power -- that SWBT now wishes to use to compete unfairly in long distance while solidifying its monopoly stranglehold over local customers.

For these and other reasons discussed below, SWBT's premature entry into the long-distance market would damage the existing robust competition in the interexchange market. At least equally important, its premature entry would shatter the fragile prospects for local competition. Congress plainly intended the prospect of long-distance entry to be an incentive to the BOCs to eliminate their stranglehold on the local market. Take that away, and SWBT will lose the only business incentive it has to cooperate with competitive local exchange carriers ("CLECs") to open the local market to competition.

As a competing local exchange provider that has already invested more than \$1 billion in local exchange facilities nationwide, and that will invest an additional \$700 million by year end, *see* Affidavit of David Agatston, ¶ 4 (ex. A hereto), MCI has a vital interest in ensuring that local markets are opened to competition in practice -- not simply on paper. In March, 1996, MCI notified SWBT that MCI wished to obtain access and interconnection throughout SWBT's region. In 1996 and continuing through MCI's recent negotiations with SWBT in Texas and Missouri, MCI requested that any final agreement with SWBT be used as a basis for negotiation of agreements in other states. Agatston Aff. ¶ 5. SWBT, however, has resisted this approach. Because of SWBT's recalcitrance, MCI was forced to demand negotiations for Oklahoma, Kansas and Arkansas, which apparently will have to proceed from scratch. *See* Agatston Aff. ¶ 5.

MCI plans to become a facilities-based provider in Oklahoma in the second half of 1998. Agatston Aff. ¶ 4. Accordingly, as a potential competitor to SWBT in the local market, MCI has a significant interest in the status of SWBT's compliance with the competitive checklist. Moreover, MCI has an important interest in the resolution of the issues of statutory construction raised by SWBT's premature application. If SWBT's filing is not dismissed as facially deficient, it will allow the Commission to establish critical precedent to govern the BOCs' proper implementation of the Act.

For these reasons, SWBT's application should be denied.

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## **ARGUMENT**

### **I. SOUTHWESTERN BELL'S APPLICATION FAILS TO SATISFY THE THRESHOLD REQUIREMENTS OF § 271.**

Section 271 imposes the burden of proof squarely on SWBT. The FCC must deny the application unless SWBT has proven that all the conditions of section 271 are satisfied. The pivotal language of subsection (d)(3) -- "The Commission shall not approve the authorization requested . . . unless it finds . . ." -- unequivocally directs the Commission to deny the application when it is unable to make the affirmative findings detailed in subparagraphs (d)(3)(A)-(C).

#### **A. SWBT Must Show that It Has Provided and Fully Implemented Each of the Checklist Items.**

The Act makes actual competition the precondition to BOC in-region long-distance entry. Specifically, section 271(c)(1)(A), known as "Track A," requires that

- (1) the BOC enter into one or more agreements approved under § 252 with a competing carrier;
- (2) the competitor actually provide service to both residential and business customers; and
- (3) the competitor provide such service exclusively or predominantly over its own facilities.

Additionally, a BOC proceeding under Track A must actually be "providing access and interconnection pursuant to one or more agreements described in paragraph (1)(A)."

§ 271(c)(2)(A)(i)(I). In order to ensure competition in the local market prior to BOC in-region entry into the long-distance market, Congress further required that the access or interconnection